Report

of the

Examination of

Physicians Insurance Company of Wisconsin, Inc.

Madison, Wisconsin

As of December 31, 2004

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, *Governor*
Jorge Gomez, *Commissioner*

Wisconsin.gov

125 South Webster Street • P.O. Box 7873
Madison, Wisconsin 53707-7873
Phone: (608) 266-3585 • Fax: (608) 266-9935
E-Mail: information@oci.state.wi.us
Web Address: oci.wi.gov

August 23, 2005

Honorable Jorge Gomez
Secretary, Midwestern Zone, NAIC
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, a compliance examination has been made of the affairs and financial condition of:

PHYSICIANS INSURANCE COMPANY OF WISCONSIN, INC.
Madison, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Physicians Insurance Company of Wisconsin, Inc., (the company) was conducted in 2001 as of December 31, 2000. The current examination covered the intervening period ending December 31, 2004, and included a review of such 2005 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations and included the following areas:

History
Management and Control
Corporate Records
Conflict of Interest
Fidelity Bonds and Other Insurance
Employees' Welfare and Pension Plans
Territory and Plan of Operations
Affiliated Companies
Growth of Company
Reinsurance
Financial Statements
Accounts and Records
Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

Independent Actuary's Review

An independent actuarial firm was engaged under a contract with the Office of the Commissioner of Insurance. The actuary reviewed the adequacy of the company’s loss and loss adjustment expense reserves. The actuary’s results were reported to the examiner-in-charge. There were no adjustments made to surplus or recommendations made in the report as a result of the actuary’s conclusion.

II. HISTORY AND PLAN OF OPERATION

Physicians Insurance Company of Wisconsin (hereinafter also, PICW or the company) was organized in 1986 pursuant to a resolution passed by the House of Delegates of the State Medical Society of Wisconsin to organize an insurance company to provide its members with medical professional liability insurance. The company's primary line of business provides the layers of health care liability insurance coverage, as required by s. 655.23, Wis. Stat., for health care providers permanently practicing or operating in Wisconsin. The limits in effect as of the annual statement date for primary coverage, pursuant to s. 655.23 (4), Wis. Stat., were $1,000,000 per occurrence and $3,000,000 per annual aggregate.

Prior to 1996, operations of the company were limited to writing professional health care liability insurance and related coverages such as commercial multi-peril and umbrella insurance in Wisconsin. The premium volume of the company's core business, medical professional liability, was being eroded by consolidation within the health care field and increased competition due to the profitability of medical professional liability insurance at that time. The company embarked on a diversification plan by entering into new lines of business covering dental professionals and small hospital facilities, marketing its products in new states, and offering high-limit deductible policies to its larger insureds.

The company is licensed to write insurance in Wisconsin, Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, Nevada, North Dakota, Ohio, and South Dakota.

In 2004, the company wrote direct premium in the following states:

Wisconsin	$39,645,817	49.9%
Iowa	19,815,047	24.9
Illinois	8,155,425	10.3
Nevada	8,070,038	10.2
Nebraska	2,431,450	3.1
Minnesota	1,127,189	1.4
South Dakota	190,197	0.2
Total	$79,435,163	100.0%

The major products marketed by the company include professional health care liability, commercial property and liability for offices of the insureds, and umbrella liability coverage. The coverages are marketed through 33 independent agencies and 3 brokers.

On July 14, 2005, the Wisconsin Supreme Court invalidated a statute capping noneconomic damages in medical malpractice cases. Medical malpractice claims are no longer subject to a statutory cap on noneconomic damages. In the case leading to the decision, the plaintiff was injured at birth. The doctor was found negligent and the plaintiff was awarded future medical and hospital expenses, and also noneconomic damages. The noneconomic damages were reduced in conformity to the statutory limit. The plaintiff appealed and the Wisconsin Court of Appeals affirmed the decision. The majority opinion of the Wisconsin Supreme Court was based on an equal protection argument. The company is currently evaluating the effect of this decision on its business, but it appears that the decision will not have an immediate adverse effect on the company's business.

The following table is a summary of the net insurance premiums written by the company in 2004. The growth of the company is discussed in the "Financial Data" section of this report

Line of Business	Direct Premium	Reinsurance Assumed	Reinsurance Ceded	Net Premium
Commercial multiple peril	$ 985,171	$	$ 553,343	$ 431,828
Medical malpractice - occurrence	16,385,927		2,624,319	13,761,608
Medical malpractice - claims made	58,773,403		17,040,247	41,733,156
Other liability - occurrence	3,290,662		2,053,988	1,236,674
Surety		2,517		2,517
Total All Lines	$79,435,163	$2,517	$22,271,897	$57,165,783

Certain guidelines apply to claims-made policies. Generally, coverage is provided if a claim is reported during the policy related to medical incidents that occurred between the retroactive date and the expiration date of the policy. Occurrence policies provide coverage for medical incidents that occur within the policy term regardless of when they are reported. An extended reporting endorsement and a death, disability, and retirement clause offered by the company have the effect of converting the claims-made policy to an occurrence policy when coverage is discontinued. Claims-made policies account for 74% of direct written premiums and occurrence policies account for 26%.

III. MANAGEMENT AND CONTROL

Ownership

There are currently 19,555 shares of Class A Common Stock outstanding which are primarily owned by past and present policyholders and officers and directors of the company. On November 4, 2004, the company's board of directors adopted a stockholders' rights plan and declared a dividend distribution of one right for each outstanding share of the company's common stock to stockholders of record at the close of business on November 15, 2004. Each right entitles its holder, under the circumstances described below, to purchase from PICW one share of common stock exercisable at a 50% discount, subject to adjustment. The rights, which expire in 10 years, become exercisable and trade separately from the common stock only upon the "distribution date," which occurs upon the earlier of:

- 10 days following a public announcement that a person or group of affiliated or associated persons has acquired, or obtained the right to acquire, beneficial ownership of 15% or more of the company's outstanding shares of common stock, or
- 10 business days following the commencement of a tender offer or exchange offer which, if consummated, would result in a person or group becoming an acquiring person.

Board of Directors

The board of directors consists of twelve members. Four directors are elected annually to serve a three-year term. Officers are elected at the board's annual meeting. Members of the company's board of directors may also be members of other boards of directors in the holding company group. The board member and committee member meeting fee schedule is as follows:

Position	**Quarterly Fees**
Chairman of the Board	$5,000
Vice-Chairman of the Board	4,500
Board Directors	3,000
	Per Meeting Fees
Committee Chairman	1,200
Committee Member	1,000
Teleconference of 1 Hour	500
Teleconference greater than 1 Hour	1,000
Mileage Reimbursement	$.405 per mile

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Steven C. Bergin, M.D. Stevens Point, Wisconsin	Obstetrician/Gynecologist Rice Medical Center/Ministry Health	2006
Ronald H. Dix Cudahy, Wisconsin	Senior Vice President Administration and Human Resources Badger Meter, Inc.	2008
Kevin T. Flaherty, M.D. Wausau, Wisconsin	Ophthalmologist Eye Clinic of Wisconsin	2007
William J. Listwan, M.D. West Bend, Wisconsin	Physician Aurora Health Center	2006
Karen B. Maclay Milwaukee, Wisconsin	Senior Vice President of Finance Advanced Healthcare SC	2006
Carol M. Meils, M.D. Fox Point, Wisconsin	Director of Cardiology All Saints Healthcare System.	2008
William T. Montei Middleton, Wisconsin	President and Chief Executive Officer Physicians Insurance Company of Wisconsin	2006
Andrew J. Policano Ph.D. Irvine, California	Dean of Graduate School of Management University of California, Irvine	2007
Thomas A. Reminga, M.D. Milwaukee, Wisconsin	President Infinity Health Care	2008
Richard G. Roberts, M.D., J.D. Verona, Wisconsin	Physician and Professor University of Wisconsin Medical School	2008
Ayaz M. Samadani, M.D. Beaver Dam, Wisconsin	Physician Dean Care	2007
Michael A. Wilson Brookfield, Wisconsin	President and Chief Executive Officer International Foundation of Employee Benefit Plans	2007

Officers of the Company

The officers serving at the time of this examination are as follows

Name	Office	2004 Compensation
William T. Montei	President	$356,014
Christopher J. Brady	Secretary	157,682
David L. Maurer	Treasurer	253,881
William S. Heck	Vice President	172,715
Kerry M. Kravik	Vice President	139,579
Penelope R. O'Hara	Vice President	164,669
Andrew F. Ravenscroft	Vice President	153,813
Helen E. Woodfall	Vice President	111,868

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Finance & Investment Committee
Ronald H. Dix, Chair
Timothy T. Flaherty, M.D.*
Karen B. Maclay, M.D.
Andrew J. Policano, Ph.D.
Ayaz M. Samadani, M.D.

Claims Committee
William J. Listwan, M.D., Chair
John Blackwood, M.D.*
Kevin T. Flaherty, M.D.
William Koller, M.D.*
Carol M. Meils, M.D.
Thomas A. Reminga, M.D.
Richard G. Roberts, M.D., J.D.
Kenneth M. Viste, Jr., M.D.*

Governance Committee
William J. Listwan, M.D., Chair
Ronald H. Dix
Carol M. Meils, M.D.
Richard G. Roberts, M.D., J.D.
Michael A. Wilson

Underwriting and Risk Management Committee
Richard G. Roberts, M.D., J.D., Chair
Steven C. Bergin, M.D.
Kevin T. Flaherty, M.D.
Timothy T. Flaherty, M.D.*
William J. Listwan, M.D.
Ayaz M. Samadani, M.D.
Kenneth M. Viste, Jr., M.D.*

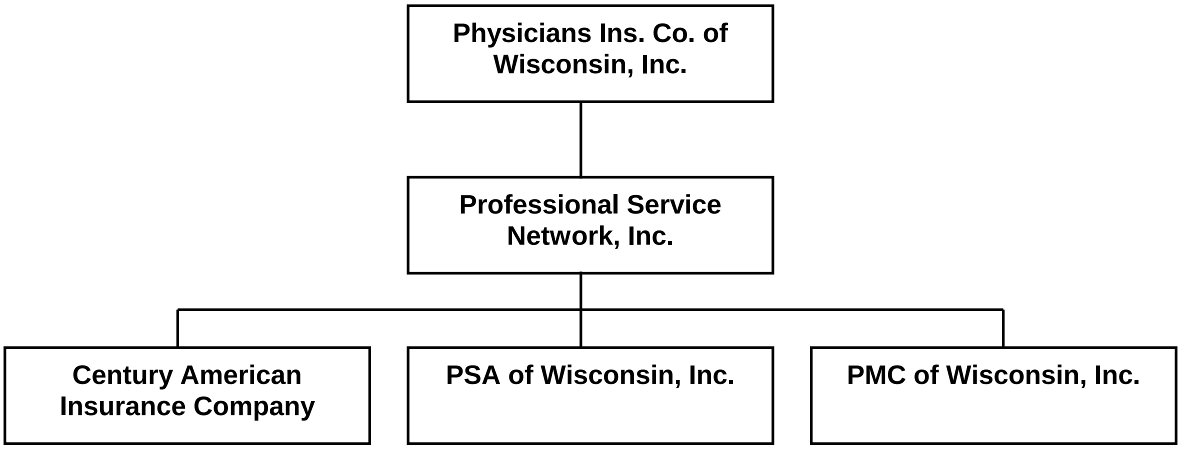
Audit Committee
Michael A. Wilson, Chair
Ronald H. Dix
Karen B. Maclay, M.D.
Andrew J. Policano, Ph.D.

* Non-director members of board committees provide advice and participate in the discussions and work of the board committees but do not vote. None are employees of the company.

IV. AFFILIATED COMPANIES

Physicians Insurance Company of Wisconsin, Inc., is the ultimate controlling person of its holding company system. The organizational chart below depicts the relationships among the affiliates in the group. A brief description of the affiliates follows the organizational chart.

Organizational Chart
As of December 31, 2004



Professional Services Network (PSN)

PSN was incorporated under the laws of Wisconsin in 1991 to provide a holding company for the subsidiaries of PICW. Effective October 1, 2004, PSN sold Century American Casualty Company (CACC) for approximately $6.7 million in cash. As a part of the sale, PICW signed a service agreement and a wraparound reinsurance agreement with CACC. Under the service agreement PICW agreed to administer ongoing surety bond business, existing medical malpractice and surety claims and reinsurance recoveries and provide financial information necessary to complete statutory statements. PICW received $450,000 in consideration for this service agreement, which will be earned over three years on a straight-line basis. Under the wraparound reinsurance agreement, PICW agreed to reinsure all the liabilities for policies written before October 1, 2004, in addition to reinsuring future surety business.

As of December 31, 2004, PSN’s financial statement reported assets of $5,887,052, liabilities of $1,420,302, and stockholders’ equity of $4,466,751. Operations for the year produced net loss of $244,666.

Century American Insurance Company

In May of 1998, Professional Service Network, Inc., acquired 100% of the outstanding common stock of Century American Insurance Company (CAIC). CAIC is domiciled in Tennessee and is also licensed in Delaware, Florida, and North Carolina. Prior to going into run-off, both CAIC and its subsidiary, CACC, primarily wrote medical professional liability policies. As of December 31, 2000, operations for both companies were in run-off status and minimal business was written. On October 1, 2004, CACC was sold by PSN to an outside party, as described above.

PICW entered into a service agreement with CAIC to provide claims, accounting, and management services. As part of the consolidation process, CAIC entered into an indemnity reinsurance agreement with CACC. CAIC cedes 100% of the outstanding loss and loss adjustment expense reserve to CACC and then PICW assumes 100% of the combined run-off business.

As of December 31, 2004, the company's audited financial statement reported assets of $5,620,780, liabilities of $54,718 and policyholders' surplus of $5,566,062. Operations for 2004 produced a net loss of $9,013.

PSA of Wisconsin, Inc. (PSA)

PSA was incorporated under the laws of Wisconsin in 1986 to function as a premium financing vehicle for business written by the company. However, PSA is currently dormant. As of December 31, 2004, PSA's financial statement reported assets of $55,807, liabilities of $158 and stockholders' equity of $55,649.

PMC of Wisconsin, Inc. (PMC)

PMC was incorporated under the laws of Wisconsin in 1986 as a management company which provided the initial capitalization for PICW. PMC's investment in PICW was replaced by policyholders who became shareholders. PMC was sold to PICW in 1988 and is currently marketing third-party claims administration services for medical malpractice business. As of December 31, 2004, PMC's financial statement reported assets of $178,504, liabilities of

$104,714, and stockholders’ equity of $73,790. Operations for the year produced net income of $63,347.

Agreements with Affiliates

The company has an agreement with CAIC to provide claims, accounting, and management services for an adjustable monthly fee. These costs have been allocated to various expense categories based on the services provided by the company.

The company has a Tax Sharing Agreement effective August 1995, whereby PICW and its subsidiaries file consolidated federal income tax returns. The method of allocation between companies is subject to the terms of this agreement, which was approved by the board of directors. Allocation is based upon separate return calculations with current credit of new operating losses or other items utilized in the consolidated return. Intercompany tax balances are settled annually.

V. REINSURANCE

The company's reinsurance portfolio and strategy is described below. A list of the companies that have a significant amount of reinsurance in force at the time of the examination follows. The contracts contained proper insolvency provisions.

Nonaffiliated Ceding Contracts

1. Type: Primary Excess of Loss

Reinsurers:	30.000%	Transatlantic Reinsurance Company
	16.321	Various Syndicates at Lloyd's of London
	10.000	Berkley Insurance Company
	12.953	Hannover Ruckversicherungs
	10.363	Alea London LTD
	10.363	Wellington Reinsurance CLTD
	5.000	Axis Reinsurance Company
	5.000	Odyssey America Reinsurance Corporation

Scope: Business classified as individual professional liability issued to physicians, mental health counselors, CRNAs, and allied health care providers; entity professional liability issued to facilities (including long-term care exposure and facilities), or groups of physicians, mental health counselors, CRNAs, and allied health care providers; all coverage afforded under the liability sections of professional office package policies issued to medical and dental practitioners; all coverage afforded under all sections of general liability policies issued to hospitals and other medical or dental facilities.

Retention: $500,000

Coverage: (A) In respect to each and every loss—$1.5 million excess of $500,000 of ultimate net loss per loss for one defendant.

(B) In respect to two or more policies and/or insured(s) involved in the same loss occurrence—$1.5 million excess of $1 million ultimate net loss per occurrence.

Maximum combined recoverable for occurrence policies, new and renewal, is 10% of gross net written premium (GNWP).

Notwithstanding the above, PICW shall retain, by way of a "Contingent Loss Corridor," an aggregate amount equal to 5.5% of GNWP of loss and loss adjustment otherwise recoverable in excess of an aggregate amount of paid loss and loss adjustment expense recovered of 13.636% of GNWP. Above that amount recoveries are unlimited.

Premium: Deposit premium is paid throughout the contract year. The actual premium paid is a sliding percentage with a minimum and a maximum premium.

Provisional premium is adjusted on a cumulative contract period basis 12 months after period end and is further adjusted at annual intervals thereafter until all losses are finally settled or commuted.

Commissions: 10% for primary excess ($500,000 xs $500,000)

Effective date: January 1, 2004

Termination: Contract may be terminated by either party sending to the other, by certified mail, written notice stating time and date of termination, which shall be effective not less than 120 days after the mailing date.

2. Type: Excess of Loss

Reinsured: General Reinsurance Corporation

Scope: Business classified as medical professional liability for physicians, surgeons, dentists, allied health care providers, and health care facilities written on a claims-made basis or, only with respect to class one dentists, on an occurrence basis; related corporate medical professional liability HMO/managed care entity liability written on a claims-made basis or, only with respect to class one dentists, on an occurrence basis; related general liability (including coverage under professional office package) either claims-made or occurrence basis; and claims-made basis umbrella and excess liability, or only when there is no professional exposure insured, on an occurrence basis. Such insurance shall be written in Kansas, Illinois, Iowa, Minnesota, Nebraska, Nevada, South Dakota, and Wisconsin.

Retention: Professional and General Liability
Individual providers (physicians, surgeons, etc.)
$1 million each occurrence
$3 million aggregate
Nebraska Fund participants: $500,000 each occurrence and $1,000,000 aggregate

Healthcare Facility Professional Liability
$1 million each and every occurrence
Nebraska Fund participants: $500,000 each occurrence and $3,000,000 aggregate

Corporate Medical Professional
$1 million each occurrence
$3 million aggregate

General Liability (Professional Office Package)
$1 million each occurrence
$2 million aggregate

Nebraska Underlying Limits clause for those residents enrolled in the state fund

Underlying Automobile and Employers Liability Limits
Automobile—combined single limit of $1 million/occurrence
Employers (Part 2 of worker's compensation and employers liability insurance policy) Wisconsin—bodily injury by accident or disease $100,000, by disease $500,000 policy limit. All other—$500,000/occurrence, $500,000 policy limit, $500,000 per employee.

	Coverage:	Policy limits greater than $1 million
		First Layer—80% of $2 million each occurrence/$2 million aggregate. PICW retention—20%
		Second Layer—100% of $3 million each Occurrence/$3 million aggregate
		Adjustment expense—pro rata basis
	Premium:	First Layer—80% of subject written premium Second layer—100% of subject written premium
	Commissions:	22.5% of reinsurance premium
	Effective date:	January 1, 2005
	Termination:	Contract may be terminated on any anniversary date with 90 days' prior written notice by either party.
3.	Type:	Excess of Loss
	Reinsured:	General Reinsurance Corporation
	Scope:	Business classified in the NAIC annual statement as medical malpractice (occurrence and claims-made). Other liability occurrence and claims-made and commercial multi-peril (property and liability coverage). Such insurance shall be written on insureds in Illinois, Iowa, Minnesota, Nebraska, Nevada, South Dakota, and Wisconsin.
		Cover A—Claims first made under death, disability and retirement (DDR) endorsements issued (claims-made basis) on or after December 31, 2003, provided endorsements are issued on claims-made policies in force at December 31, 2003, and including new claims-made policies in 2004.
		Cover B—Occurrences taking place (as respects occurrence basis) and claims first made (claims-made basis) January 1, 2004, and prior to January 1, 2005, policies in force on January 1, 2004 (2004 term).
		Cover C—Awards made against PICW from January 1, 2005, to December 31, 2005, for losses in excess of policy limits and extra contractual obligations.

	Coverage:	(A) 100% up to $8.6 million. (B) 100% in excess of an 85% retention of subject net earned premium up to $3.5 million (2004 term) and 100% in excess of 68% of subject 2005 net earned premium up to $3.5 million, but the liability of the reinsurer is not to exceed $4.9 million. (C) 100% up to a maximum of $2 million. The liability of the reinsurer on all coverages under this contract shall not exceed $12.5 million.
	Premium:	A flat rate is paid for each of the coverages listed above.
	Effective date:	December 31, 2003
	Termination:	Contract may be terminated by either party sending to the other, by certified mail, written notice stating time and date of termination, which shall be effective not less than 120 days after the mailing date.
4.	Type:	Property Quota Share
	Reinsurer:	13.39% Wellington Reinsurance Ltd. 61.61 Various Syndicates at Lloyd's of London
	Scope:	Property sections of professional office package policies issued by the reinsured to medical and dental practitioners.
	Limits:	Maximum of $4,000,000 any one risk and $3,000,000 any one building, with a proportionate share of loss adjusting expenses. Reinsured percentage per risk 75%, ceding company retention per risk 25%.
	Premium:	Proportionate share of original gross net written premium.
	Commissions:	22.5%
	Contingent commissions:	25% of reinsurer's net profit by formula from the contract during each underwriting year.
	Effective date:	January 1, 2004
	Termination:	Contract may be terminated on any anniversary date with 90 days' prior written notice by either party.

VI. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2004, annual statement. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

Physicians Insurance Company of Wisconsin, Inc.
Assets
As of December 31, 2004

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$207,265,713	$	$207,265,713
Stocks:			
Common stocks	31,734,519		31,734,519
Real estate:			
Occupied by the company	2,691,793		2,691,793
Properties held for the production of income	540,000		540,000
Cash	(266,818)		(266,818)
Short-term investments	5,354,402		5,354,402
Investment income due and accrued	1,128,863		1,128,863
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	4,688,673	43,714	4,644,959
Deferred premiums, agents' balances, and installments booked but deferred and not yet due	12,430,685		12,430,685
Reinsurance:			
Amounts recoverable from reinsurers	288,983		288,983
Current federal and foreign income tax recoverable and interest thereon	2,806,322		2,806,322
Net deferred tax asset	6,964,180	2,994,229	3,969,951
Guaranty funds receivable or on deposit			
Electronic data processing equipment and software	2,190,679	1,986,009	204,670
Furniture and equipment, including health care delivery assets	267,143	267,143	
Receivable from parent, subsidiaries, and affiliates	878,480		878,480
Other assets nonadmitted	28,753	28,753	
Write-ins for other than invested assets:			
Prepaid expenses	657,134	657,134	0
Amounts receivable under high deductible policies	1,234,568		1,234,568
Prepaid asset	1,784,388	1,784,388	
Bishops Bay equity certificates	33,000	33,000	0
Accounts receivable other	47,342		47,342
Total Assets	$282,748,802	$7,794,370	$274,954,432

Physicians Insurance Company of Wisconsin, Inc.
Liabilities, Surplus, and Other Funds
As of December 31, 2004

Losses		$ 83,627,976
Reinsurance payable on paid loss and loss adjustment expenses		(1,286)
Loss adjustment expenses		57,176,482
Commissions payable, contingent commissions, and other similar charges		1,612,392
Other expenses (excluding taxes, licenses, and fees)		1,869,333
Taxes, licenses, and fees (excluding federal and foreign income taxes)		(149,502)
Unearned premiums		19,193,200
Advance premium		6,009,736
Ceded reinsurance premiums payable (net of ceding commissions)		642,425
Funds held by company under reinsurance treaties		14,892,084
Amounts withheld or retained by company for account of others		1,598
Write-ins for liabilities:		
Deferred service revenue		440,369
Retroactive reinsurance reserve		299,110
Surety escrow deposits		40,541
Total Liabilities		185,654,458
Common capital stock	$ 6,581,858	
Surplus notes	12,000,000	
Gross paid in and contributed surplus	10,887,108	
Unassigned funds (surplus)	70,031,739	
Less treasury stock, at cost:		
Common	(10,200,731)	
Surplus as Regards Policyholders		89,299,974
Total Liabilities and Surplus		$274,954,432

Physicians Insurance Company of Wisconsin, Inc.
Summary of Operations
For the Year 2004

Underwriting Income		
Premiums earned		$56,488,655
Deductions:		
Losses incurred	$20,090,745	
Loss expenses incurred	26,722,631	
Other underwriting expenses incurred	12,448,709	
Total underwriting deductions		59,262,085
Net underwriting gain or (loss)		(2,773,430)
Investment Income		
Net investment income earned	5,819,084	
Net realized capital gains or (losses)	1,979,223	
Net investment gain or (loss)		7,798,307
Other Income		
Net gain or (loss) from agents' or premium balances charged off	(5,983)	
Write-ins for miscellaneous income:		
Service fee income	20,039	
Net gain on sale of equipment	460	
Retroactive reinsurance loss	(643,275)	
Miscellaneous income	52,730	
Total other income		(576,029)
Net income (loss) before dividends to policyholders and before federal and foreign income taxes		4,448,848
Dividends to policyholders		1,108,982
Net income (loss) after dividends to policyholders but before federal and foreign income taxes		3,339,866
Federal and foreign income taxes incurred		236,474
Net Income		$ 3,103,392

Physicians Insurance Company of Wisconsin, Inc.
Cash Flow
For the Year 2004

Premiums collected net of reinsurance			$ 55,260,267
Net investment income			6,536,881
Miscellaneous income			(576,028)
Total			61,221,120
Benefit- and loss-related payments		$ 7,926,728	
Commissions, expenses paid, and aggregate write-ins for deductions		31,902,052	
Dividends paid to policyholders		1,108,982	
Federal and foreign income taxes paid (recovered)		(196,853)	
Total deductions			40,740,909
Net cash from operations			20,480,211
Proceeds from investments sold, matured, or repaid:			
Bonds	$111,243,998		
Stocks	24,680,462		
Net gains (losses) on cash and short-term investments	672		
Miscellaneous proceeds	427,592		
Total investment proceeds		136,352,724	
Cost of investments acquired (long-term only):			
Bonds	165,778,461		
Stocks	16,743,852		
Total investments acquired		182,522,313	
Net cash from investments			(46,169,589)
Cash from financing and miscellaneous sources:			
Surplus notes, capital notes		12,000,000	
Capital and paid-in surplus less treasury stock		(304,580)	
Other cash provided (applied)		(4,875,377)	
Net cash from financing and miscellaneous sources			6,820,043
Reconciliation			
Net change in cash and short-term investments			(18,869,335)
Cash and short-term investments, December 31, 2003			23,956,920
Cash and short-term investments, December 31, 2004			$ 5,087,585

Physicians Insurance Company of Wisconsin, Inc.
Compulsory and Security Surplus Calculation
December 31, 2004

Assets		$274,954,432	
Less security surplus of insurance subsidiaries		2,800,000	
Less liabilities		185,654,458	
Adjusted surplus			$86,499,974
Annual premium:			
Medical malpractice	$54,388,778		
Factor	50.0%		
		27,194,389	
Lines other than accident and health	1,668,023		
Factor	33.3%		
		555,452	
Total		27,749,841	
Compulsory surplus (subject to a minimum of $2 million)			27,749,841
Compulsory surplus excess (or deficit)			$58,750,133
Adjusted surplus (from above)			$86,499,974
Security surplus: (140% of compulsory surplus, factor reduced 1% for each $33 million in premium written in excess of $10 million, with a minimum factor of 110%)			38,572,278
Security surplus excess (or deficit)			$47,927,696

Physicians Insurance Company of Wisconsin, Inc.
Reconciliation and Analysis of Surplus
For the Four-Year Period Ending December 31, 2004

The following schedule is a reconciliation of total surplus during the period under examination as reported by the company in its filed annual statements:

	2004	2003	2002	2001
Surplus, beginning of year	$76,300,301	$65,362,288	$69,077,829	$74,693,514
Net income	3,103,392	2,506,738	(6,288,155)	3,826,974
Net unrealized capital gains or (losses)	1,499,705	3,884,334	3,402,533	(2,308,173)
Change in net deferred income tax	403,566	83,029	1,819,708	198,557
Change in nonadmitted assets	(3,741,430)	3,651,889	(2,050,806)	(2,573,387)
Change in provision for reinsurance		742,224	(742,224)	
Change in surplus notes	12,000,000			
Cumulative effect of changes in accounting principles				618,064
Capital changes:				
Paid-in	4,805	6,628	14,650	(382,573)
Transferred to surplus	1,669,848			
Surplus adjustments:				
Paid-in	42,106	63,173	136,288	539,471
Transferred from capital	(1,669,848)			
Change in treasury stock	(351,490)		(7,534)	(5,534,619)
Write-ins for gains and (losses) in surplus:				
Transfer of nonadmitted receivables on sale of CACC	39,019			
Rounding		(2)	(1)	1
Surplus, end of year	$89,299,974	$76,300,301	$65,362,288	$69,077,829

Physicians Insurance Company of Wisconsin, Inc.
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2004

The company's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below. Unusual IRIS results are denoted with asterisks and discussed after the table.

	Ratio	2004	2003	2002	2001	2000
#1	Gross Premium to Surplus	89%	107%	103%	64%	41%
#2	Net Premium to Surplus	64	77	75	47	35
#3	Change in Net Writings	(2)	19	52*	24	24
#4	Surplus Aid to Surplus	1	3	1	1	0
#5	Two-Year Overall Operating Ratio	98	101*	94	77	78
#6	Investment Yield	2.5*	3.0*	4.0*	5.8	4.2*
#7	Change in Surplus	18	14	(4)	(7)	(4)
#8	Liabilities to Liquid Assets	72	76	77	70	64
#9	Agents' Balances to Surplus	5	5	8	0	0
#10	One-Year Reserve Development to Surplus	(5)	19	(3)	9	13
#11	Two-Year Reserve Development to Surplus	8	12	(14)	14	22
#12	Estimated Current Reserve Deficiency to Surplus	22	56	14	12	13

In 2002, the exceptional result for Ratio #3, "Change in Net Writings," was primarily due to increased writings in existing markets. The low investment yields during the period under examination are generally reflective of trends in market interest rates. The unusually low investment yield for 2004 was also reflective of higher than usual investment expense related to the issuance and placement of a $12,000,000 surplus note. In 2003, the exceptional result for Ratio #5, "Two-Year Overall Operating Ratio," was attributed to premium growth and low investment yields.

Growth of Physicians Insurance Company of Wisconsin, Inc.

Year	Admitted Assets	Liabilities	Surplus As Regards Policyholders	Net Income
2004	$274,954,432	$185,654,458	$89,299,974	$3,103,392
2003	244,538,121	168,237,820	76,300,301	2,506,738
2002	203,552,041	138,189,755	65,362,288	(6,288,155)
2001	182,710,910	113,633,080	69,077,829	3,826,974
2000	166,429,556	91,736,043	74,693,514	5,295,635

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss And LAE Ratio	Expense Ratio	Combined Ratio
2004	$79,437,680	$57,165,783	$56,488,655	82.9%	22.8%	105.7%
2003	81,914,848	58,626,576	61,878,642	90.5	17.5	108.0
2002	67,449,459	49,154,901	40,287,060	96.1	21.4	117.5
2001	43,916,101	32,349,922	30,353,106	76.3	32.1	108.4
2000	30,798,588	26,020,203	22,650,115	60.0	36.2	96.2

Since the last examination as of December 31, 2000, assets have increased by $108.5 million or 65.2%, liabilities have increased by $93.9 million or 102.4%, and surplus increased by $14.6 million or 19.6%. The decline in surplus in 2002 was mainly attributable to an underwriting loss of $8.9 million, offset by a net investment gain of $3.0 million along with a change in nonadmitted assets of $2.1 million. The investment gain was due to $6.6 million investment income offset by $3.6 million realized capital loss. Substantially the entire 2003 and 2004 earned premium relates to medical malpractice liability insurance, which is provided primarily using claims-made policies. Approximately 50% and 47% of the company’s 2004 and 2003 direct written premiums, respectively, were written in Wisconsin and 25% and 23% were written in Iowa.

Reconciliation of Surplus per Examination

No adjustments were made to surplus as a result of the examination. The amount of surplus reported by the company as of December 31, 2004, is accepted.

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were five specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the company are as follows:

1. Investments—It is recommended that the company add indemnification clauses to its custodial investment agreement in order to enhance the safeguard of securities.

   Action—Compliance.

2. Cash Controls—It is recommended that the company destroy old check stock in order to avoid duplication problems.

   Action—Compliance.

3. Expense Allocation—It is recommended that the company formally document the methods employed to provide a basis for the calculation of expense allocations.

   Action—Compliance.

4. Premium—It is recommended that the company establish reports that indicate how amounts from the policyholder level detail are incorporated into the deferred premium calculation.

   Action—Compliance.

5. Premium—It is recommended that the company properly account for due and uncollected premium amounts and establish the appropriate accrual in the annual statement.

   Action—Compliance.

Summary of Current Examination Results

This section contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

Disaster Recovery Plan

The examination noted that the company was continually updating its business resumption plan, but the last evidence of testing the plan provided by the company was in the year 2000. Testing validates the viability of the plan. It is recommended that the company continue to update its business resumption plan to properly address issues necessary to continue operations in the event of a disaster, and test its business resumption plan at least annually.

Current Federal and Foreign Tax Recoverable and Interest Thereon

The company reported the current year receivable on the annual statement as a consolidated balance for "Current Federal and Foreign Income Tax Recoverable and Interest Thereon." The federal tax balances due from its subsidiaries were reported on the line items for "Receivables from Parent, Subsidiaries and Affiliates" and "Payable to Parent, Subsidiaries and Affiliates." The NAIC Annual Statement Instructions – Property/Casualty state that amounts owed due to intercompany tax-sharing agreements are to be excluded from the annual statement lines for "Receivable from Parent, Subsidiaries and Affiliates" and "Payable to Parent, Subsidiaries and Affiliates." The company should only report tax and affiliated balances in accordance with SSAPs 10 and 25. The company has changed its procedures for reporting federal income taxes during the 2005 reporting year to be consistent with the NAIC Annual Statement Instructions – Property/Casualty and SSAPs 10 and 25.

Affiliated Balances

In reviewing the current year and subsequent year settlements of affiliated service agreements, it was noted that the company settles its affiliated balances on an as-needed basis and that one balance due from an affiliate had been outstanding without settlement since the prior exam. Although these amounts are immaterial in nature, the agreements with the stated payment terms were submitted and approved by the commissioner. It is recommended that the company settle its affiliated balances on a timely basis in accordance with the applicable agreements filed with and approved by the commissioner.

Subsequent Events

On September 21, 2004, American Physicians Capital, Inc., and American Physicians Assurance Corporation filed a Form A, which described a plan to acquire 4,450 shares of common stock in Physicians Insurance Company of Wisconsin, Inc., representing approximately 22.7% of the shares issued and outstanding, from five current shareholders at a purchase price of $3,800 per share in cash. The Form A was subsequently amended to propose the purchase of an additional 332 shares from another shareholder, thereby increasing the amount of the proposed acquisition to approximately 24% of the shares outstanding.

The company expressed the view that the proposed acquisition of shares constituted a hostile takeover attempt. The company, the six shareholders that were seeking to sell their shares to the applicants and the Wisconsin Medical Society filed motions for status as a party to the proceeding. The applicants and the company filed motions and briefs concerning requests for and the conduct of discovery. On July 20, 2005, Commissioner Gomez issued a Decision on Standing and Discovery that:

- Granted the company's request for admission as a party.
- Determined that it was unnecessary to further examine the status of the six selling shareholders or the Wisconsin Medical Society given their expected limited participation. For purposes of discovery, each of them was to be treated as a party.
- Applicants' and PICW's requests for discovery were granted subject to qualifications as to scheduling and procedure.

Discovery by applicants and PICW proceeded and the exchange of documents was accomplished. On August 30, 2005, the Office of the Commissioner of Insurance (OCI) sent a list of interrogatories to the applicants. On August 31, 2005, the applicants notified the OCI of the termination of the Stock Purchase Agreement and indicated a decision on their part to withdraw the Form A. On the same day, without prior notice to the OCI, American Physicians Assurance Corporation executed new stock purchase agreements with five of the six shareholders who had been party to the previous stock purchase agreement whereby it purchased 1,942 shares, representing approximately 9.93% of PICW's issued and outstanding shares.

On September 7, 2005, the applicants filed a motion for the Commissioner to terminate the proceeding for lack of subject matter jurisdiction. On the same day, Commissioner Gomez issued a Pre-Hearing Conference Memorandum that:

- Directed the applicants and PICW to reserve September 28, 2005, for a possible pre-hearing conference to address scheduling and other pending matters.

- Directed that the applicants' motion to dismiss the proceeding, and PICW's objection, would be addressed by briefs and supporting material with respect to the following questions: 1) May the applicants unilaterally terminate this Class 1 proceeding which was initiated under ch. 227, Wis. Stat., to consider the applicants' plan under s. 611.72, Wis. Stat., and ch. 617, Wis. Stat., and 2) Does OCI retain jurisdiction to conduct a Class 1 proceeding under ch. 227, Wis. Stat., to determine the nature of applicants' plan, which includes the applicants' August 31, 2005, acquisition of 9.93% of PICW's voting stock?

- Directed the applicants to respond to OCI's inquiry dated August 30, 2005, by October 7, 2005.

On October 31, 2005, Commissioner Gomez denied the applicants' motion for termination for lack of subject matter jurisdiction. Representations and supporting documents demonstrated that there are genuine and material issues of fact in dispute as to whether the applicants continue to have a plan to acquire control after the termination of the original stock purchase agreement. In addition, the Commissioner concluded that the applicants had not demonstrated that it was appropriate, at this late stage in the proceeding, to approve voluntary dismissal of the case.

On December 21, 2005, ProAssurance Corporation filed a plan to acquire all the outstanding shares of common stock in Physicians Insurance Company of Wisconsin, Inc. The definitive agreement calls for each share of PICW stock to be converted into shares of ProAssurance stock necessary to produce a value of $5,000 per share of PICW stock. The exchange ratio is based on the average closing price of a share of ProAssurance stock on the ten trading days preceding the effective date of the merger.

On January 13, 2006, Commissioner Gomez approved a Stipulation, Joint Motion and Proposed Order suspending the proceeding regarding the plan for the acquisition of control of

PICW by American Physicians Capital, Inc., and American Physicians Assurance Corporation, pending a decision upon the application by ProAssurance Corporation.

Both cases are pending before the Office of the Commissioner of Insurance.

VIII. CONCLUSION

Since the last examination as of December 31, 2000, assets have increased by $108.5 million or 65.2%, liabilities have increased by $93.9 million or 102.4%, and surplus increased by $14.6 million or 19.6%. Substantially the entire 2003 and 2004 earned premium relates to medical malpractice liability insurance, which is provided primarily using claims-made policies. Approximately 50% and 47% of the company's 2004 and 2003 direct written premiums, respectively, were written in Wisconsin and 25% and 23% were written in Iowa.

Effective October 1, 2004, Century American Casualty Company was sold by Professional Service Network, Inc. (a subsidiary of Physician Insurance Company of Wisconsin, Inc.) for approximately $6.7 million in cash. As a part of the sale, PICW signed a service agreement and a wraparound reinsurance agreement with CACC.

On November 4, 2004, the company's board of directors adopted a stockholders' rights plan and declared a dividend distribution of one right for each outstanding share of the company's common stock to stockholders of record at the close of business on November 15, 2004. Each right entitles its holder, under the circumstances described below, to purchase from PICW one share of common stock at the exercise at a 50% discount, subject to adjustment. The rights, which expire in 10 years, become exercisable and trade separately from the common stock only upon the "distribution date," which occurs upon the earlier of:

- 10 days following a public announcement that a person or group of affiliated or associated persons has acquired, or obtained the right to acquire, beneficial ownership of 15% or more of the company's outstanding shares of common stock, or
- 10 business days following the commencement of a tender offer or exchange offer which, if consummated, would result in a person or group becoming an acquiring person.

There are two separate proposals to acquire common shares of PICW pending with the Office of the Commissioner of Insurance.

On July 14, 2005, the Wisconsin Supreme Court invalidated a statute capping noneconomic damages in medical malpractice cases. Medical malpractice claims are no longer subject to a statutory cap on noneconomic damages. The company is currently evaluating the effect of this decision on its business. It appears that the decision will not have an immediate adverse effect on the company's business.

The current examination noted that the company complied with all of the prior recommendations. The current examination report made two recommendations. The current examination did not make any reclassifications of accounts or adjustments to surplus. As a result of the examination, the company's admitted assets, liabilities, and stockholders' equity were as follows:

Admitted assets	$274,954,432
Liabilities	185,654,458
Stockholders' Equity	$ 89,299,974

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 27 - Disaster Recovery Plan—It is recommended that the company continue to update its business resumption plan to properly address issues necessary to continue operations in the event of a disaster, and test its business resumption plan at least annually.

2. Page 27 - Affiliated Balances—It is recommended that the company settle its affiliated balances on a timely basis in accordance with the applicable agreements filed with and approved by the commissioner.

X. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Name	Title
Jerry DeArmond	Insurance Financial Examiner – Advanced
Randy Milquet	Insurance Financial Examiner – Advanced
Eleanor Oppriecht	Insurance Financial Examiner – Senior
Rebecca Easland	Insurance Financial Examiner
Andrew Fell	Insurance Financial Examiner

Respectfully submitted,

Russell Lamb
Examiner-in-Charge